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An analysis of Wisconsin's new venture capital and early stage finance programs

Gregory J. Lynch and Chad R. Taylor,

If high tech is the engine of future economic growth, Wisconsin is running low on investment “fuel.” A recent study by the California-based Milken Institute ranks our state 32nd out of 50 in availability of the risk capital that technology entrepreneurs need to turn innovative ideas into marketplace successes. That may soon change thanks to the recent enactment of 2003 Wisconsin Act 255 by Governor Doyle.

Act 255 encourages angel investors and venture capitalists to invest in Wisconsin high tech companies, and helps those companies secure federal and third party funding. Although the Wisconsin Department of Commerce must still resolve a number of questions, its two key provisions – investment tax credits, and a grant and loan program – hold real promise to generate new sources of investment that emerging companies need for growth.

Investment Tax Credits

Act 255 creates two tax credit programs for early stage seed investments and angel investments, both to be overseen and administered by the Department of Commerce. Commerce must certify that the credits go to qualified new business ventures which:

- Is headquartered in Wisconsin
- Employ less than 100 people, and at least 51% of those are in Wisconsin
- Is engaged in, or has committed to engage in, manufacturing, agriculture, or processing or assembling products and conducting research and development or developing a new product or business process
- Is not engaged in traditional financial, consulting, professional services, retailing, hospitality, construction or transportation activity
- Have been operated in Wisconsin for not more than seven consecutive years
- Have not received more than \$1 million in investments that qualify for angel tax credits

The Early Stage Seed Investment Credit against individual and corporate income and franchise taxes is equal to 25% of the initial investment paid to an investment fund manager to invest in qualified new business ventures in any taxable year, beginning after December 31, 2004. There is a \$35 million

maximum for all combined credits claimed in all tax years. Partnerships, limited liability companies or tax-option corporations may not claim the credit, and Commerce must certify that fund managers are eligible to accept and properly invest venture capital.

The Angel Investment Tax Credit authorizes an individual angel investor to receive an income tax credit of up to 12.5% of any bona fide angel investment, to a maximum of \$500,000 for each investment made in any two consecutive taxable years beginning after December 31, 2004. The maximum allowable aggregate credit amount is \$30 million for all tax years. Investments are defined as the purchase of an equity interest or other expenditure in qualified new business ventures, made by an individual or network of individuals who regularly review new businesses for potential investment.

Commerce must publicly list the eligible venture investors and qualified new business ventures that it certifies, and make an annual report on investment activity. Act 255 also requires Commerce to define what expenditures other than equity investments constitute bona fide angel investments, and to develop rules limiting angel investments to \$3 million per year and venture investments to \$3.5 million per year.

Grant and Loan Program

The second key element of Act 255 is the creation of a Technology Commercialization Grant and Loan Program funded at \$2.6 million annually. It is administered by the Department of Commerce to ensure that grant recipients are located and grants are spent in Wisconsin and that the applicants are viable. The program authorizes five types of grants and loans:

- *Early Stage Planning* grants and loans, to cover up to \$15,000 in professional services needed to apply for federal R&D funding or to achieve business objectives required by third party investors. Recipients must have enough other funding to cover at least 25% of total project costs.
- *Matching* grants and loans of up to 20% of project costs or \$250,000 (whichever is less) to fund professional services that help a recipient develop or commercialize innovative products, processes or services. Recipients must either have secured, or be about to secure, federal funding to bolster their efforts.
- *Bridge* grants and loans of up to 75% of project costs or \$100,000 (whichever is less) to tide recipients over until they receive third party financing or federal grants to develop or commercialize their innovations.
- *Venture Capital* grants and loans of up to 50% of project costs or \$250,000 (whichever is less) to enhance recipients' ability to secure early stage third party financing.
- *Entrepreneurial & Technology Transfer Center* grants of up to \$500,000 a year to finance centers that serve multiple regions of Wisconsin by providing entrepreneurs with planning, intellectual property, referral and similar business development services.

Two key points to re-emphasize about these Technology Commercialization Grants and Loans. First, they are supplemental funding. Applicants and recipients must be small businesses or entrepreneurs who have applied for or are waiting to receive federal grants for early stage R&D funding or early stage third party financing. And second, the Wisconsin Department of Commerce must confirm that applicants are viable and that their innovative products or services are primarily developed in or sold from this state.

With similar restrictions in place for the investment tax credits, it may take a while to generate substantial momentum among small and emerging businesses to take advantage of the full program. But, thanks to Act 255, the fuel for growth is there – and all of Wisconsin will benefit.

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Law Practice:

Greg Lynch is a partner with Michael Best & Friedrich where his principal experience has been in the following areas:

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- Mergers and acquisitions
- Early-stage company and venture capital representation
- General corporate law, including corporate governance and 1934 Act compliance

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Mr. Lynch has served as corporate counsel to a variety of multinational clients and has assisted in structuring, negotiating and integrating acquisitions in North America and Europe. Mr. Lynch has also represented national, regional and local clients in a variety of other corporate transactions, including public offerings, private placements, corporate financing, venture capital financing and corporate governance. Mr. Lynch also represents early stage and emerging growth companies and investors in corporate structuring and financing. Prior to his private practice, Mr. Lynch has served as an extern for Justice Andrew G.T. Moore of the Delaware Supreme Court, where he worked on a variety of Delaware corporate law and corporate governance matters.

Professional Activities:

- Member, Board of Advisors University of Wisconsin Weinert Applied Ventures in Entrepreneurship
- Member, American Bar Association
- Member, State Bar of Wisconsin, Business Law Section

Admissions:

- Wisconsin, 1998
- Illinois, 1994

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Education:

- University of Iowa (J.D., high distinction, 1994, Member, Order of the Coif and *Journal of Corporation Law*)
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Law Practice:

Chad Taylor is an associate practicing in the firm's Land & Resources Law Group. Mr. Taylor concentrates his practice in the area of government relations and lobbying, providing strategic counseling on legislative, public policy and regulatory matters to corporate, municipal and trade association clients. He also practices in the areas of administrative, public contract, election, ethics and campaign finance law. Mr. Taylor formerly served as Chief Legal Counsel to the Office of the Governor, Chief Legal Counsel & Senior Policy Advisor to the Office of the Assembly Speaker and as an intern for the Wisconsin Supreme Court. Mr. Taylor has also served as Chairperson of the Wisconsin Pardon Advisory Board and as a member of the Wisconsin Claims Board and the Governor's Taskforce on Terrorism Preparedness.

Professional Activities:

- Member, Association of Wisconsin Lobbyists
- Executive Committee, Member, Waukesha County Republican Party, 2002-present
- Board Member, Zoological Society of Milwaukee County - Associate Board
- Member, Association of General Contractors, Legislative Committee, 1999-2001, 2003-present
- Chief Legal Counsel, Office of the Governor, 2001-2002
- Wisconsin Pardon Advisory Board, Chairperson, 2001-2002
- State Claims Board, Member/Governor's Appointee, 2001-2002
- Governor's Task Force on Terrorism Preparedness, Member, 2001-2002
- Chief Legal Counsel and Senior Policy Advisor, Office of the Assembly Speaker, 1997-1999
- Member, Waukesha Area Chamber of Commerce, Government Relations Committee, 1999-2001

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Admissions:

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